

**THOMAS R. SMITH, CPA**  
**CERTIFIED PUBLIC ACCOUNTANT**

15 November, 2013

Board of Directors  
SunEagle Bay Owners Association Incorporated  
P.O. Box 359  
Yantis, Tx. 75497

RE: Limited Scope Audited Financial Statements For the 3 Years Ended June 30, 2013

Dear Ladies and Gentlemen:

First of all, I would like to take this opportunity to thank the Board for the opportunity to work with SunEagle Bay and I look forward to providing other information that is needed by the Board and the Association.

The intent of the engagement was not to render an opinion on the financial statements when taken as a whole, but rather to look at the procedures used by the Board(s) and the receipts and disbursements to make sure that they were adhering to the policies, rules and laws as discussed in the engagement letter. Among other things, I performed the following tests and tasks related to the audit:

- Read all of the minutes of the Board and Annual meetings held during the years under examination and subsequent to June 30, 2013. This period would be from July 1, 2010 through July 31, 2013.
- Examined all of the bank statements from BankTexas from June 30, 2010 through September 30, 2013 as well as the bank account reconciliations prepared by the third party bookkeeper for the fiscal year ends. The period was expanded to determine existing liabilities and commitments prior to the beginning of the audit and to determine subsequent events and unrecorded liabilities as of the ending balance sheet date.
- Reviewed billing details reports (accounts receivable) and traced them into the general ledger.
- Made test selections of specific transactions from the general ledgers received directly from BTP services for all of the periods under examination.
- Reviewed documentation available regarding the TCEQ allegations that were open at the June 30, 2010 and verified closure without penalty or exposure to the Association.
- Discussed internal controls and processes for billing, cash collections, cash disbursements, asset acquisition and contracting. This included related party transactions.

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- Read the By-Laws and Deed Restrictions of SunEagle Bay Owners Association, as amended.
- Examined the original invoices and details of paid receipts for selected cash disbursements.
- Compared financial results on a year by year basis for irregularities and fluctuations.
- Questioned third party bookkeeper regarding procedures, specific transactions and general ledger, including any reports to the governmental authorities that have been or are required to be filed.
- Reviewed various correspondence files to determine contingencies and issues which could impact the financial statements.
- Reviewed the Federal income tax returns for the years ended June 30, 2010 – 2012. The return for the year ended June 30, 2013 is on extension and is due in February, 2014.
- Reviewed the insurance policies in effect to review coverage and adequacy of limits.
- Discussed with Board members and the third party bookkeeper the procedures and controls regarding cash receipts and disbursements, billing, accounts receivable and collections, purchases and accounts payable, and fixed asset control.
- Examined annual billings to members based on ownership records to determine accuracy of billing.
- Traced selected receipts from check copies through deposits to bank to the general ledger.
- Reviewed select records from the Wood County clerk regarding transfers, foreclosures and liens (collection efforts).

Based on the results of the work performed, I can advise the Board and the Association of the following:

- All checks written since July 1, 2010 have been signed by two signers.
- Support exists for disbursements made by check, including reimbursements to directors and members for personal money spent by them on behalf of the Association. These reimbursements were primarily for repair parts, supplies, and postage.
- Cash and checks received are properly accounted for and put into the Association's bank account.
- I found nothing in any of the work performed that would indicate that any of the money disbursed was for anything except the benefit of the SunEagle Bay Owners Association or that any Board member has profited from their position on the Board.

- I found nothing that would indicate that any member of the Board has breached his or her fiduciary responsibility to the membership of the Association.
- While not an attorney, I found nothing that would indicate that so far as the management of the Association is concerned, the Board has done anything not permitted by the By-Laws. Currently, the Association is not in compliance with portions of Section 209 of the Texas Property Code. The Board is aware of the non compliance and is working to bring the Association into compliance.
- I found no disbursements that were for liabilities of any other organization or paid for goods and services not received by the Association.
- I found substantiation for all cash expenditures selected for examination. The substantiation supported the amount and account distribution within the general ledger.
- The recommendations for adjustments made at the last examination have not been made. It appears that these got lost as insignificant with all that has been going on a SunEagle Bay.

The purpose of this engagement is to fulfill the requirement in the By-Laws for an audit every three years. As was described in the prior audit report, the records of the Association as they relate to certain balance sheet accounts (as discussed below) are not auditable. The Association is more interested in the cash flow components of the financial activity on an annual basis than in some of the historic items. Accordingly, the focus of this audit is on the dues and assessments billed and collected and the validity of the amounts paid and to whom the money was paid. The spirit and intent of the By-Laws with regard to an audit has, in my opinion, been fulfilled with the approach taken.

The purpose of an audit is to express an opinion about whether or not the financial statements express fairly the financial position of the Association and the results of operations for a specified period in **accordance with generally accepted accounting principles (GAAP), consistently applied.** Generally Accepted Accounting Principles are a complex set of rules requiring disclosures either on the face of the financial statements or in the footnotes to the financial statements. Since its beginning in 1986, the Association has been focused on the cash that came in and the cash that has been spent. Detail records regarding fixed assets and non cash expenses required to be disclosed to have a comprehensive method accounting acceptable in GAAP have not been maintained. The Association uses for its management purposes a cash basis income statement (cash received and cash spent), which is adequate for daily management of cash flow but provides an incomplete view.

Accordingly, it is not practical for the Association to have an audit as defined by the American Institute of CPA's (AICPA) in accordance with Generally Accepted Auditing Standards (GAAS). These standards are designed for audits to be done annually since many of them require work to be done at each Balance Sheet Date presented. It is not that these things can not be done multiple years at a time, but with the condition of the balance sheet records, it becomes more difficult and very impractical. There are general ledger accounts that require attention if the Association desires to put itself in a position to have an audited financial statement. That being said, audits are usually

done because they are required by financial institutions, lenders, regulatory agencies or for other specific reasons, including the anticipated sale of a Company or a law or regulation that requires an audit of a governmental agency. As explained in the engagement letter, an audit when done in accordance with GAAS, **may or may not** discover fraud or misuse of funds . But work has been done to evaluate the internal controls of the Association and make recommendations for changes that will strengthen the overall financial operations of the Association

With regard to the review of internal controls and operating procedures, I would make the following recommendations in addition to the accounts previously mentioned:

- Job Descriptions for each officer and Board member position needs to be written, reviewed by the Board and put into the records of the Association. Each Board member, before accepting a position as an officer should read and sign a copy of the job description. The job descriptions should be detailed enough so that responsibility for each topic for management of the Association is assigned to Board members as primary and backup.
- Written procedures for each major process needs to be written and approved by the Board. These processes would include but not be limited to purchasing, check writing, collections, filing, requirements for minutes and budgeting as examples. As officers change, the procedures should stay in place until approved by the Board. This is not to say that the incoming officer does not have a better idea as to how to do something, but rather to leave a trail as a starting point for the next person doing the job.
- Prior to any check being signed, the person who receives the good or service should sign the vendor invoice indicating that the good or service has been received and is acceptable. I understand we are talking about a small group of people authorized to purchase on behalf of the Association, and that before checks are written, work performed is verified. By signing the vendor invoice, if a question ever arises, it becomes easy to see who did and who approved the work or received the part. This is being done on some invoices, but not consistently.
- Each year, an operating budget should be prepared for the subsequent year and presented to the membership at the annual meeting for approval. I understand that this recommendation has been implemented, but the minutes of meetings do not have any copies of the budget and the monthly reports do not show actual performance versus the budget. None of the budgets for the 3 years of the examination and the current year ( year ending June 30, 2014) are in the Quickbooks. This will accomplish the following:
  - The membership will have input into the Board's plans for managing the Association for the following year.
  - The monthly financial reports can include a comparison on both a monthly and year to date basis of actual results to the budgeted amounts. This will help the Board monitor the actual results as compared to the budget.

- Variances can be explained on the report and that will become a part of the Association's permanent record.
- Contract Labor should be done by written contract. There is potential liability to the Association if there is not sufficient documentation to prove to the IRS, if asked, that these are contractors, not employees.
- Director Liability Insurance. Directors' Liability insurance should be explored and obtained. The Corporate documents provide some protection, but an insurance policy would be advisable.
- Accounting policies should be reduced to writing. This relates primarily to capitalization policies, useful lives of assets, revenue recognition, establishment of reserves for doubtful accounts. The reasons have been discussed above.
- As noted above, the adjustments recommended at the last audit have not been made. The Board should review the adjustments recommended at the last audit and instruct the third party accounting firm to make the adjustments to the ledger.
- During the previous examination, copies of checks and cash received were made at the office prior to delivery to the accounting office where deposit tickets were made and the checks are posted to the books. This procedure has been terminated during the current examination period. It is recommended that the procedure be reimplemented and that the Treasurer verify that copies made equal the deposits shown on both the bank statements and the financial statements on a monthly basis.
- During the prior examination, it was recommended that the accounts payable files (check stubs and original invoices) should be cleaned and reorganized. It was noted during the current examination that this was done and much improved.
- Should the Board decide to reinstate the petty cash account, checks made out to reimburse the petty cash account should be made payable to the custodian of the account, not to cash. For example, the proper way would be to make reimbursement checks payable to "Jane Doe, Petty Cash Custodian". One person should be responsible the account and it should be kept under lock and key. I would recommend against reestablishing a petty cash account.
- The revenue of the Association has decreased annually for the last several years based on billing. The reason for this is that the existing owners are purchasing additional lots as they come available. The Association assesses dues on a sliding scale based on the number of lots owned. As the ownership consolidates, the revenue to the Association decreases. Consideration should be given to modifying the ByLaws to either eliminate or at a minimum reduce the sliding scale to bolster the revenue of the Association. Assets are ageing and will require replacement and there is no significant cash reserve to pay for these replacements.
- Each lot at SunEagle Bay has road frontage. The policy of the Association is to asses each member equally for road repairs and improvements. Arguments can be made on both sides

of this policy, but in two of the last three years, more money has been spent on roads than has been brought in through the assessments. The recommendation is to review the policy and make changes necessary to insure the ongoing viability of the property under the control of the association.

I have not audited the Balance Sheets of SunEagle Bay Owners Association Incorporated and the related Statements of Income and Changes in Fund Balance for the years ended June 30, 2013, 2012 and 2011 in accordance with Generally Accepted Auditing Standards and express no opinion on the financial statements taken as a whole. However, based on the work performed, it is my opinion that the Board is meeting its fiduciary obligations, managing within the parameters of the Articles of Incorporation and the By-Laws, assessments collected are properly recorded in books and deposited in the Association's bank accounts and cash disbursed is used to fulfill the obligations of the Association and for the benefit of the members. From a financial statement perspective, I noted no misuse of funds. Further, the Board has improved the accounting and reporting function over prior years and is showing inclination to further improve the financial statements.

If you have any questions or would like further information, please do not hesitate to contact me.

Best Regards,

Thomas R. Smith, CPA  
Mineola, Tx.